

WESTERN UKRAINE INITIATIVE

LAND O'LAKES, INC.
International Development Division

**CROSS BORDER TRADE AND RELATED ISSUES
PERTAINING TO THE
DEVELOPMENT OF THE AGRICULTURAL SECTOR IN
WESTERN UKRAINE**

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Country of location: Ukraine
Dates of Assignment: March 16 to April 10, 1999

TASK ASSIGNMENT AND SCOPE OF WORK

1. In conjunction with the current phase of the Western Ukraine Initiative (WUI), Land O'Lakes engaged a short term consulting assignment to assess the current cross border trade issues between Ukraine and Poland/Hungary that may impact the further development of agriculture in the western region of Ukraine. The underlying purpose of this assignment was to provide USAID with a strategic reassessment of its approach toward agricultural reform in western Ukraine, policy issues which need to be addressed and changes that might warrant further consideration at the regional level to expand the agricultural sector in this geographic area.

2. Accordingly, the purpose of this memorandum is to summarize the observations made during this assignment, and provide comment and recommendations to LOL and USAID with respect to cross border trade and related issues which could positively impact the ongoing development of the agricultural sector in western Ukraine.

3. Meetings were held in Washington with LOL's Deputy Director of Operations, ACDI, USDA-FAS Multilateral Trade Negotiation Division, USAID Office of Enterprise Development for Europe/NIS, USDA Economic Research Service and USDA-FAS Deputy Director of Commodity of Analysis. In country travel in Poland consisted of meetings with local businesses, USDA Agricultural Attache in Warsaw, local/regional trade development organizations, and one regional agricultural chamber of commerce. In Ukraine, numerous meetings were held in L'Viv and the surrounding region with local private businesses, venture capital and banking representatives, regional farmer organizations, Honorary Counsel of the Netherlands, and staff representatives of LOL, ACDI and USAID. Final meetings were held in Kiev with international trade companies engaged in the export of agricultural products, the USDA Agricultural Counselor, The World Bank, a USAID supported agricultural input supplier, and one storage/processing company.

BACKGROUND

4. Cross border trade issues are only one of several inter-related factors that impact the effectiveness of the USAID program in western Ukraine. In addressing cross border trade it is important to view the development of agriculture in western Ukraine in a much broader context. While specific cross border trade issues are important and need to be addressed in order to develop a more transparent, commercially oriented marketplace, the review of the underlying business environment in western Ukraine, including government policy, market structure, rural finance, cultural issues and the reality of the current regional market structure, all have significant impact on the further development of the agricultural sector in western Ukraine. Each of these inter-related factors either directly or indirectly impact cross border trade issues, which in combination have an overall influence on the development of western Ukrainian agriculture.

5. Under the old system prior to 1939, agricultural production in western Ukraine was organized around a localized social structure that emanated from the involvement of individuals at the village or community level. Even though there were large landowners that utilized local producers on an as-needed basis, community groups came together to pool their resources to create local production enterprises (cooperatives). These groups were the basis by which local producers operated as a cohesive economic unit. This provided a mechanism to raise capital, purchase necessary capital goods (which a single producer could neither afford nor justify on an individual basis), and market output, both locally as well as to more distant terminal markets. Under this structure, a linkage of trust and financial participation was in place which connected the small land owner/producer directly to the source of inputs as well as the marketing point for output production. The relationship was one of community participation and involvement, where the group monitored and influenced the performance and commitment of each individual member of the group. This form of operation was an efficient and effective means of providing local support as well as insuring the commitment and responsibility of each small producer to the overall benefit of the group.

6. World War II brought an entirely new structure into the marketplace. Contrary to the continuation of individual farm ownership in Poland, Ukrainian farmland was nationalized and converted into large state farms. Community involvement and individual responsibility to the group was no longer the driving force at the local level. Instead, orders came from the central government, as well as the supply of inputs, the decisions concerning what would be produced, and the destination of production output. Decisions were no longer made by the individual producer or their local group, but instead by the central government. This mentality of central, governmental control of enterprise management and decision making, and the resulting lack of individual responsibility and involvement, was the primary result of Soviet agricultural policy in Ukraine.

7. Another issue that is pertinent to the comparison of agriculture in Ukraine versus Poland is the identity of the people. Whereas Poland is made up primarily of families of Polish origin, where small farms have been held in the same family for many generations (even through the Soviet era), Ukraine is a melting pot of Ukrainians, Russians, Poles, Hungarians and other ethnic groups which migrated to Ukraine subsequent to the 1939 partition agreement reached between Hitler and Stalin. Although Ukraine does have a strong national heritage, the people of Ukraine do not have the same 'one country' image of themselves as is the case in Poland. Further, the recent privatization of state owned farm land has resulted in the creation of a large population of small scale subsistence farmers and non-farmer land owners. The majority of this group had no prior connection to the ownership of a specific parcel nor a long standing involvement with the local community as is the case in Poland. In L'Viv Oblast alone it is estimated that there are currently around 750,000 such small individual land owners and producers.

8. The economic policy initiated in Poland after the break-up of the Soviet Union allowed this country to rapidly adjust its infrastructure, legal system and marketplace toward

a more progressive system of government and free enterprise. Although this has caused serious hardship in certain sectors, the results have been for the most part positive. Farmers, food processors, marketing companies and related support enterprises are able to operate in the marketplace under a progressive rule of law, with the availability reasonably priced commercial credit and access to production inputs, machinery, etc. on a readily available basis. On the contrary, Ukraine's approach to post-Soviet economics has been slow, cautious, and not focused on the serious restructuring of the governmental agencies and policies, the financial sector, and legal structure. Even though the two countries share a common border and ethnic background, there is a marked difference between the two, including trade related regulations, attitude toward trade in general, the support of the government toward producer organizations (such as Polish farm unions), and the difference in governmental perspective toward expansion versus tight control of agricultural production. In Poland the government has taken the approach of encouraging production increases with subsidies and other supportive governmental policies, under the theory that higher production will provide the country (and the government) with lower prices and higher tax revenues in the long run. On the contrary, Ukraine has adopted an ever increasing regime of regulatory controls, obsessive taxes, and other governmental policies which stifle production and reduce incentive in the private sector to take business risks which in a free market economy would be weighed against the potential profits that could be earned by increasing output, starting new enterprises, recycling capital, etc.

9. With the break-up of the Soviet Union and the large flow of economic aid into this region from many foreign governments including the USA, there has been an emphasis toward supporting changes that will result in immediate economic and structural improvements. In certain countries, such as Poland and Hungary, which have strong feelings of national identity and closer ties to Western Europe, this aid has had significant positive impact. These results can be measured in the economic progress that has been made in these countries, as well as their comparatively rapid political evolution toward democratic, free market systems of government and commerce. On the other hand, in countries such as Ukraine where the agricultural sector was formerly organized as large, non-descript state owned farms and whose people are a mixture of many different nationalities and ethnic groups, foreign aid has had significantly poorer results. With the question constantly being asked "*what can we do different in Ukraine to get more meaningful results from our AID programs ?*", it should be noted that in this country one is dealing with a different (i.) social structure, (ii.) connection to the land, (iii.) relationship of individual to local community and government, and (iv.) the proximity as well as commercial access to western markets.

10. It is with the above background and context that the review of cross border issues was made. In addition to specific policies that were felt to be relevant to cross border trade between western Ukraine and Poland/Hungary, comment and recommendation have also been made concerning related factors that might warrant further evaluation by LOL and USAID in the next phase of the Western Ukraine Initiative.

CROSS BORDER TRADE - UNDERLYING CONSIDERATIONS

11. Several observations were made during this assignment that pertain to the issue of cross border trade as well as the more general development of agriculture in western Ukraine in conjunction with USAID's ongoing strategy. The combined interaction of these factors have a significant impact on the business climate in western Ukraine, which in turn impact the development of the agricultural sector.

12. Trade imbalance: It is important to note that there currently exists a major imbalance in the sale of agriculture products between Ukraine and Poland. Although similar statistics were not gathered for Hungary, it is suspected that the same situation exists there as well. The question was repeatedly asked concerning what agricultural products could be sold from Ukraine to Hungary and Poland. The trade of inputs and machinery from Poland/Hungary to Ukraine is limited only by available capital on the part of the Ukrainian buyer/importer. Except for regular regulatory and procedural issues which appear to be dealt with in the normal course of trade, shipment of these items into Ukraine do not appear to be a problem. On the other hand, shipment of almost any form of agricultural product from Ukraine into Poland or Hungary meets with serious regulations and other road blocks. Trade in small, individual automobile lots of consumer goods appears to be thriving, although large tonnage sales of meats, grains, oilseeds and dairy products are for the most part non-existent from east to west. Although statistics were not available for the 1998 calendar year, the following numbers reflect a significant trend in cross border trade and the corresponding trade policies that are currently in effect.

TOTAL AGRICULTURAL PRODUCTS – POLAND/UKRAINE			
	<u>1995</u>	<u>1996</u>	<u>1997</u>
Poland to Ukraine	\$103	\$165	\$220
Ukraine to Poland	\$ 36	\$110	\$ 34
USD 000,000's			
Source: USDA - FAS Global Agricultural Trade System			

13. Central budget: Because Ukraine currently does not have a strongly structured national budget, each governmental agency relies to a large part on fee revenue generated by each such entity. This applies to the local and regional level, as well as at the national level. Such a structure encourages local decisions to be made which result in extra charges, changes in procedural requirements and a confusing mix of rules and regulations. While some Ukrainian importers indicated that this was not a serious issue and was dealt with as a normal part of doing business, the lack of a comprehensive national budget and the ability to fund agencies from general tax revenues encourage local bribery and spontaneous changes in rules and regulations.

14. Farm debt to the federal government: In many of the privatized enterprises, including former state farms as well as processing enterprises, old debt presumably owed to

the government continues to be carried as an ongoing obligation. This has resulted in confiscation of production output, attachment of sales proceeds and similar collection procedures, which have a significant impact on the newly structured enterprise's ability to continue operations. The debt issue should be addressed at the federal level in such a way that provides buyers, lenders and marketing companies, as well as the producer who is carrying the debt, with a clearly defined means of determining what must be paid and at what time, through the life of a specific commercial transaction. Conversion of this debt to some other form of financial instrument should also be given consideration, as its continued existence will have ongoing negative impact on the enterprise's ability to secure financing, enter into sales contracts, and similar commercial activities.

15. Role of Government of Ukraine in the marketplace: Although not particularly significant for items such as fresh produce, dairy and meat products, there does occur from time to time governmental intervention into the marketplace with respect to the confiscation of certain products at below-market prices for national food security purposes. While such a policy is understandable and in certain instances justified, it has a negative impact on how foreign buyers as well as companies engaged in the export of these commodities view the reliability of sales being made from Ukraine into the international marketplace. Consideration should be given to some means of registering export transactions, which once so registered, would remain in effect and allow the transaction to move forward without interference. In the event the product from such a transaction was required to remain in country for national security reasons, a provision should be made whereby the corresponding export contract can be bought back from the overseas buyer which previously purchased this product, with the seller/exporter being compensated for difference between the price it ultimately received from the Ukrainian Government and the price established in the original transaction. Such a contract protection mechanism would enhance Ukraine's standing in the international marketplace, ultimately providing a stronger and more competitive domestic market where prices would more closely relate to world market conditions.

16. Ukrainian farmer's perception of government: As commented previously, the structure of the agricultural sector in Ukraine during the Soviet Union resulted in a heavy reliance on the 'government' toward all phases of agricultural production and marketing. Although many new farmers and entrepreneurs recognize that they are now independent and cannot rely on the government to supply inputs, make production decisions and provide marketing outlets, there still exists an expectation that government should be doing more to assist the agricultural sector. While in many countries, including the USA, governmental support (both financial and non-financial) has had many positive impacts to the agricultural sector, there appears to be widespread confusion on the part of many Ukrainian producers and processors over what the government should do, what it realistically can do, and what it should not do, in supporting Ukrainian agriculture. There are many conflicting and contradictory policies at the federal as well as regional and local level, which create a confused and often frustrating situation. For instance, the Information Research Center in L'Viv has been organized to provide production inputs, market output, create a marketing center and eventually a commodity market, for the L'Viv Oblast. This quasi governmental organization, although created perhaps with the best of intentions, could potentially

perpetuate the old central planning mentality, slowing the efforts of USAID toward the development of a profitable, competitive, transparent agricultural sector.

17. Rule of law: The general commercial atmosphere in Ukraine, including existing laws, new regulations, control of crime, the collection of debt, and creditor priority in a judicial proceeding all inhibit the ability of commercial enterprises to function and prosper. Instead of supporting and providing encouragement to entrepreneurs to take risks, expand production, seek new markets, and reinvest earnings, the legal and regulatory structure in Ukraine act as major inhibitors toward the increase in production output and development of cross border trade.

18. Market liquidity and recognition of different market sectors: It should be noted that there are substantial differences in western Ukraine concerning how different agricultural products are marketed, who the primary buyers are, in what quantity increments these products are sold, and what impact these factors have in the sale of these various product categories to countries such as Poland and Hungary. Given the fact that most farms in western Ukraine are very small operations and in many cases operate on a quasi-subsistence basis, each of these operators are producing several products of varying quality and packaging, in very small quantities. For example, one farmer may be growing one hectare of potatoes, one hectare of sugar beets, one hectare of cabbage, two cows, six pigs, etc. This level of production results in the sale of small sale increments (individual automobile, wagon or truck loads), which are generally made on a cash or barter basis. This form of production and marketing does not lend itself toward the development of an established, transparent marketplace which allows for forward contracting, payment advances, firm, fixed prices for future delivery at the time of harvest, and uniform standards for quality and packaging. All of these factors are significant when considering the sale of Ukrainian agricultural products to other countries, as well as into the domestic marketplace. Emphasis should be given to the difference between such small scale production of many different items raised by one farming enterprise (with many of these products being perishable fruits and vegetables), as compared to more uniform, non-perishable items such as wheat, rapeseed, corn, barley, etc., that can be sold in larger quantities, forward contracted, organized for delivery in multi-truck or rail car lots, and handled much more efficiently by a marketing organization. All of the above factors impact market liquidity as well as the optimum market destination to which a producer should be selling.

19. Sale of farm-direct production versus processed goods: Further to the previous point of market liquidity, a distinction should be made between product which can and is being sold direct from the farm to the end customer versus sale to a processor, such as a meat company, cheese manufacturer, flour miller/baker, cannery, etc. The food processing sector in western Ukraine appears to be growing and there is evidence of significant interest from many companies and individuals in the organization and operation of processing enterprises. These processing units represent a secondary but important market level, as they create competition in the local market place, allow individual producers to sell their output in relatively small increments directly to the processor, and in many cases, convert the primary product which may be a perishable item or a live animal, into a form which can be

held in storage and delivered over relatively long distances to other markets, either inside Ukraine or to other countries.

20. Terms of sale: Depending on the structure of a particular transaction, the product being bought and sold, the monetary value, terms and method of payment, relationship between buyer and seller, and whether the business is occurring on a local basis versus across international borders, there are different methods used to decrease or in some cases eliminate taxes, duties, fees and related charges. Many different scenarios were described by companies which utilize different methods to reduce import/export fees and taxes. Although no opinion or judgement is intended, it should be noted that payment terms vary significantly due to the above factors. Terms of sale can and do have a significant impact on the overall feasibility of profitable commerce, particularly when product is being imported into Ukraine from Poland and Hungary.

21. Russian financial crisis: The recent banking crisis in Russia has had both a direct and indirect impact on the market for Ukrainian agricultural products. In addition to Russia being the key market for agricultural products being sold directly from Ukraine, countries such as Poland and Hungary also relied heavily on Russia as a destination for large quantities of processed food items as well as basic food stuffs. The indirect result has been serious surpluses of agricultural products being accumulated in Poland and Hungary. In Poland for instance, the Agricultural Marketing Agency (ARR) is currently buying up surplus production of meat, butter and dried milk after the serious uprising by Polish farmer unions concerning the decline in market prices and overflowing inventories backing up in the Polish marketplace. These ARR stocks will not only create a strong resistance toward the sale of similar products from Ukraine into Poland (which at the present time is almost impossible to accomplish), but will likewise create competition in the Russian market by the sale of such ARR inventories which might otherwise be an outlet for Ukrainian production.

22. United States food aid to Russia: In addition to the surpluses being created in Poland as well as other countries such as Hungary, Czech Republic and others, the donation of food products from the USA to Russia creates an additional negative effect on the primary market for Ukrainian food products. This causes reverberations back to the local market in Ukraine for companies which in the past have sold to Russia, as well as the further backup of production in Poland and Hungary. This regional backup restricts the possible indirect sale of Ukrainian production to Russia via Polish and Hungarian processing companies and well as direct sales from Ukraine to Russia.

23. Role of multi-nationals: Although not evident in the L'viv Oblast, at least during this assignment, there has been significant activity in various regions of Ukraine by large multi-national companies. Such involvement has included (i.) the supply of inputs, both directly and through local distributors, on a credit basis with payment coming from production output at the time of harvest, (ii.) the creation of input packages, including seed, fertilizer, chemicals, equipment, and so forth, which is supplied on a coordinated basis through one entity to a group of farmers or larger state owned farms, again with payment from production output, (iii.) the outright leasing of farmland by outside operators who provide

inputs, management, markets, etc., with the land owner just leasing the land, with or without the supply of local labor, and (iv.) the establishment of local processing operations which contract with local producers to supply certain products on a contractual basis to the processing company. In many instances these types of operation have been successful and have provided Ukrainians with a model of how modern, efficient agricultural methods can be profitably utilized in Ukraine. However, such an approach often may not address the social issues of small scale, community based agriculture alluded to previously, particularly if the long term goal is to strengthen rural communities, create a economically sound population of small scale producers who have access to an open, user friendly marketplace. No opinion is intended by the above. The question that should perhaps be addressed is what long term outcome is intended by USAID, i.e. the development of a strong local rural sector or large, corporate multi-national farming and production enterprises.

24. Rural credit: Underlying the entire focus on development of a profitable agricultural sector is the need for credit at the producer level. The access to such credit has direct impact on cross border trade issues. For example, if local Ukrainian producers have access to credit and can purchase necessary inputs to produce a product that is needed by a Polish processing or marketing company, this will result in completely different transaction structure versus one which requires the Polish company to enter the market with inputs on open credit, taking the production risk until the time of harvest. The feasibility of effective rural credit should be analyzed from the following viewpoints:

- Direct credit being provided to each independent producer versus cooperative lending at the local, village level.
- The financing of basic, easily monitored, bulk, non-perishable products which can be forward contracted and that have a well defined, controllable cash stream for direct repayment of short term financing.
- The realities of providing production financing to farms in Ukraine, given the current legal structure, land title system, attitude of borrowers toward lenders and vice versa, farmer business (financial) knowledge and expertise, interest rate competitiveness and lender operating costs.
- The distinct differences between one crop, short term crop/production financing versus longer term credit for machinery and related fixed asset improvements.
- Whether a potential borrower is in need only of credit, or instead, expertise in structuring the overall business enterprise, including the optimum combination of short term borrowing, long term debt, equity capital, possible purchase advances from customers, and related advantages of contractual commitments which impact the credit worthiness of the borrower with respect to lender evaluation.
- A realistic evaluation by outside sources of credit (direct funding as well as secondary guarantees) concerning the needs of the Ukrainian market, the realities

of lending money in this environment, and what is needed to create a commercially viable Ukrainian banking sector which is capable of and willing to support the credit needs of western Ukraine on a basis that allows for prudent, properly managed and profitable lending.

25. In summary, there is a wide difference between Poland and Ukraine in many areas. When taken in context, they have a significant impact on cross border trade as well as western Ukraine's ability to sustain and increase agricultural production for both domestic consumption as well as sale into the international marketplace.

CROSS BORDER TRADE ISSUES

26. In considering the particular issues that have possible impact on cross-border trade between Ukraine and Poland/Hungary, thought should be given to the true intention of the respective government in the regulation of such transactions. Particularly for Ukraine, are cross border regulations, duties, taxes and related charges intended to (i.) protect the public against inferior product quality, (ii.) insure uniformity and transparent quality guidelines for product being traded across international borders, (iii.) generate revenues at the federal level, albeit to the several different agencies which play various roles in licensing, inspection, clearance and approval of international transactions, and/or (iv.) a means of generating income at the regional, local and even individual level, using governmental regulations and involvement as a means of tolling the importer/exporter on a discretionary basis?

27. Simplification and coordination of import/export requirements: There is currently no central coordination evident in Ukraine, at least during this assignment, that has overall authority for import/export procedures, fee structure, and related activities. Certain border crossing points are noted as having relatively smooth, well established clearance policies, whereas others are considered as "running a gauntlet". However, it should be noted that in many instances if an importer is prepared to properly document their transaction, obtain pertinent pre-clearance documents, utilize a knowledgeable local customs broker, and pay established fees without attempting to doctor paperwork or bribe officials, border crossing is not an insurmountable obstacle. On the other hand, especially for smaller shipments such as consumer goods or retail packed food items in the trunk of an automobile, and where the operator is intent on minimizing customs fees, taxes, etc., there can be considerable variation in the fees charged and the difficulty encountered in crossing the border. Regardless of the border crossing point, the size of the transaction, and the intent of the shipper to adhere to versus circumvent regulations, there are numerous procedures and regulations that must be followed. Using the entry of products coming into Ukraine as an example, the following approvals and documents must be obtained, many of which come from separate governmental agencies. Depending on whether the importer has pre-cleared the shipment or intends to do this at the time of border crossing, fees can be paid after shipment following local inspection at destination in L'viv (for pre-cleared deliveries), versus inspection and payment of fees at the border for shipments which have not been pre-cleared.

- Import licensing
- Contract registration

- Certificate of Origin
- Certificate of Conformity with Ukrainian Standards
- Sanitary Certificate of Conformity with Ukrainian Standards (where applicable)
- SES Permission Certificate
- Phytosanitary Certificate (for plant materials)
- Veterinary Certificate (for livestock materials)
- Import duty
- Customs fees
- VAT tax
- Excise tax (where applicable)

28. Although the above list may not be complete, it is intended to show that there are numerous documents and procedures required to ship product from and into Ukraine. In addition, governmental import/export policy is established and updated at three levels; federal, regional and local office. Such a combination of different regulatory agencies, without central budget funding, operating on the basis of three levels of authority, often results in a confusing, time consuming and expensive process to ship goods across the borders of Poland and Hungary into Ukraine. A similar review was not made on the Polish and Hungarian side, but this should also be addressed in the overall clarification of cross border trade regulations.

29. Pre-clearing, special gates and designated crossing hours: As noted previously, all traffic, including passenger cars, small lorries, commercial trucks, etc., pass through the same gate at each border crossing. Even though trucks often have their own lane and crossing area, in most cases they must go through the same entry and exit point. Procedures should be considered to allow for pre-clearance of shipments, particularly for larger truckload or multi truckload shipments, where documentation, inspection and estimated border arrival time can be determined in advance. Perhaps a crossing period, such as midnight to early morning, for such pre-cleared shipments, would allow them to cross the border without having to pass through the same procedure as cars and trucks which have not gone through such pre-clearance procedures.

30. In-transit processing and duty drawback: Clarification and procedural details should be obtained to explore the possibility of shipping unprocessed products from Ukraine to processors in Poland and Hungary, for eventual sale to other countries such as Russia. In this instance, the processor/importer in Poland would be able to process and re-export Ukrainian origin products without having to pay import duties, customs, fees, etc., that would apply if the product was eventually sold into the Polish domestic market.

ISSUES RELATED TO TRADE AND MARKET DEVELOPMENT

31. For the foreseeable future it is not likely that changes will occur at the national level in Ukraine that will result in the strengthening of the rural agricultural sector, particularly for the small scale land owner and operator. Even though this support is needed and would presumably result in significant increases in production output as well as the financial well being of Ukrainian agriculture, change must come from the local level. Individual producers

and processors, taking the entrepreneurial initiative to expand output, develop new enterprises, deal with market conditions as they exist today, are what is needed to move development forward. Given the lack of support at the national level in Ukraine, outside support from organizations such as USAID should continue to focus on exposing and linking Ukrainian operators to counterpart contacts in Poland and Hungary. Learning by doing is a key to the development of small scale, sustainable, profitable agriculture.

32. In conjunction with exposure to counterpart operations in Poland and Hungary, as well as corresponding technical support that can be provided from a variety of sources, another key factor that needs to be stressed in the development of the agricultural sector in Western Ukraine is the refinement of marketing strategies, small scale production financing, and workable methods of tying such financing to the marketing function.

RECOMMENDATIONS

33. It was evident during this consulting assignment that considerable effort has been made in exposing Ukrainian farmers and food processors to new methods of production, marketing and financial management. While this exposure is important and should be continued, other areas that pertain to the simplification of cross border trade procedures, production financing, marketing, and strengthening of local producer groups should also be considered as additional design features for the next phase of the Western Ukraine Initiative. The following recommendations are made accordingly:

34. Cross Border Technical And Cultural Exchange: The continuation of trade fairs, interchange between Ukrainian and counterpart entities in Poland and Hungary, and the ongoing development of commercial and cultural ties should be encouraged and continued by Land O'Lakes as a key component of the next phase of the Western Ukraine Initiative. As mentioned previously, it does not appear likely that support for the western Ukraine agricultural sector will come from the Ukrainian federal government. Providing foreign aid and political pressure at the federal level will not accomplish the changes in local expertise, investor confidence, community involvement and cross border support that are necessary to increase productivity in this region of Ukraine. This must come from local producers, investors and entrepreneurs, who over time can learn the necessary technical, marketing and financial skills that are key to the operation of a successful business enterprise.

35. Cross Border Trade Procedure Handbook: Given the myriad of regulations, agencies, procedures and related tasks that are involved in conducting cross border trade between Ukraine and Poland/Hungary, a comprehensive trade handbook produced for Ukrainian producers and processors would be a helpful tool in not only defining procedures, but also in the actual purchase and sale of products between these countries. Input for such a handbook should be sought from local and regional governmental agencies, customs brokers, transportation companies, etc., from both sides of the border, so that when completed it will represent the contribution of the various interests involved with cross border trade. In addition to rules, regulations, procedures, fees, agencies, documents, and the like that are required for cross border trade, further detail should also be included which

defines the different procedures for various product categories, size of transaction, pre-clearance of transactions versus clearance at the time of border crossing, differences in procedures for different border crossing points, and suggestions that would assist a Ukrainian company in conducting business with Poland and Hungary. Another area that might warrant inclusion in this document would be possible procedures that could be followed to arrange for bulk transfers of large quantities of product, perhaps through a specific border crossing point during particular hours, days, etc., which would facilitate border crossing for such transactions. In addition to Poland and Hungary, similar information might also be provided for other crossing points that would be utilized for delivery to destinations such as Russia, Belarus, and other NIS republics.

36. Trade Finance And Marketing Component: As mentioned earlier in this memorandum, there are many inter-related factors that impact the ability of producers and processors in Western Ukraine to make correct production decisions, obtain inputs, arrange for short term financing, gain access to machinery and equipment, and successfully market output. Resistance to the sale of certain products to adjacent countries such as Poland due to the large agricultural surpluses that currently exist in such neighbouring countries, governmental regulations, taxes, old debt, legal structure, optimum production mix from a marketing standpoint, focused marketing strategy and proper financial structuring are all factors that need to be incorporated in a successful production and marketing plan. This proposed new component of the Western Ukraine Initiative would provide Ukrainian farmers and processors with exposure to the following:

- It is proposed that a small number (two or three) producer and/or processor groups be identified for participation. A production and marketing plan would be developed and supervised for each such group, including the initial steps of crop/product planning/budget forecasting, financing, obtaining inputs, forward marketing, delivery of output, collection of sale proceeds and repayment of input costs and related production financing.
- The accumulation of capital and means of holding this capital in a form which is secure and not exposed to undue taxation and other methods of collection, should all also be covered in this component. Knowing that many Ukrainian producers currently prefer to deal in barter or small scale cash transactions in order to avoid high taxes and other governmental interference, a methodology should be developed to create a more secure commercial climate which encourages sound financial management, retention of capital, and repayment of short term operating debt, all of which are important to the ongoing development of the agricultural sector in Western Ukraine.
- The possible collaboration with counterpart Polish and Hungarian companies, perhaps utilizing the concept of in-bond or duty drawback processing of unprocessed Ukrainian goods in Poland/Hungary for ultimate sale to the NIS and other markets, could be a added feature of this component. This structure could provide access to (i.) inputs advanced on credit, (ii.) other forms of short term

production financing, (iii.) a creditworthy and knowledgeable trade partner outside of Ukraine, and (iv.) a well defined marketing outlet with secure sales revenues. Such a collaborative structure, involving actual transactions with Polish and Hungarian counterparts, would provide the Ukrainian participants with an excellent “learn by doing” environment, thus encouraging the development of the agricultural sector in Western Ukraine at the individual and community level.

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